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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940.

A. B. PITTMAN, Trustee, National Cottonseed Products Corporation, Bankrupt,
Petitioner,

vs.

UNION PLANTERS NATIONAL BANK AND TRUST COMPANY, ET AL.,
Respondents.

No. 118

PETITION OF A. B. PITTMAN, TRUSTEE, NATIONAL COTTONSEED PRODUCTS CORPORATION, BANKRUPT, FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

LOWELL W. TAYLOR,
LARRY CRESON,
Attys. for Petitioner.

TABLE OF CONTENTS

Pages

PETITION OF A. B. PITTMAN, TRUSTEE, NATIONAL COTTONSEED PRODUCTS CORPORATION, BANKRUPT, FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT 1-11

Summary Statement of the Matter Involved 1-2

Proceedings in District Court, Pleadings and Issues 2-8

Reasons Relied on for Allowance of The Writ 8-10

Prayer for Writ 11

BRIEF AND ARGUMENT IN SUPPORT OF PETITION 13-46

Jurisdiction 14

Question Presented for Review 14-24

ASSIGNMENT OF ERRORS 24-25

POINTS OF LAW 25-32

ARGUMENT 33-46

TABLE OF AUTHORITIES

Table of Cases

Pages

American Can Co. v. Erie Preserving Co. (D. C.) 171 Fed. 540 (1909) 9, 26, 27, 28, 30, 39

Bank v. Ebbert & Co. (Tenn.), 9 Heiskell 153 (1872) 30, 32

Bank of Rome v. Hazelton, 83 Tenn. 216 (1885) 25, 26

Benedict v. Ratner, 268 U. S. 353, 45 S. Ct. 566 (1925) 8, 40

Coats, Bennett & Reidenbach, Re (C. C. A. 2d), 12 Fed. (2d) 497 (1926) 9, 28, 29

Collinwood Motor Sales Co., Re (C. C. A. 6th), 72 Fed. (2d) 137 (1934) 32, 40

Fleming v. Noble (C. C. A. 1st), 250 Fed. 733 (1918) 34

Fourth State Nat'l Bank v. Milbourne Mill Co's. Trustee (C. C. A. 3rd), 172 Fed. 177 (1909) 9, 27, 30, 39

General Motors Acceptance Corp. v. Green County Union Bank (Tenn.), 95 S. W. (2d) 948 (1936) 32

Hamilton Ridge Lumber Sales Corp. v. Wilson (C. C. A. 4th), 25 Fed. (2d) 592 (1928) 39

Hyman v. Semmes (C. C. A. 6th), 26 Fed. (2d) 10 (1928) 29, 39

Interstate Banking Co. v. Brown (C. C. A. 6th), 235 Fed. 32 (1916) 30, 31

Love v. Export Storage Co. (C. C. A. 6th), 143 Fed. 1 (1906) 26, 27, 28

Manufacturing Co. v. Nordeman, 118 Tenn. 384 (1906) 32

TABLE OF AUTHORITIES—Continued

Pages

Maryland Casualty Co. v. Washington L. & B. Co. (Ga.), 145 S. E. 761, 61 A. L. R. 323 (1928) 27

McGaffey Canning Co. v. Bank of America, 294 Pac. 45, 109 Cal. App. 415 ..... 27, 28, 39

Morgan Bros. v. Dayton Coal & Iron Co., 134 Tenn. 228 (1915) 32, 41

Ommen v. Tolcott (C. C. A. 2d), 188 Fed. 401 (1911) 29

Pittman, Trustee, v. Union Planters Nat'l Bk. & Tr. Co., et al, (C. C. A. 6th), 118 Fed. (2d) 211 ..... 9, 14, 43

Rogers, In Re (C. C. A. 7th), 125 Fed. 169 (1903) 9, 27, 28, 39

Security Warehousing Co. v. Hand, 206 U. S. 415, 27 S. Ct. 720, 51 L. Ed. 1117 (1907) 4, 8, 9, 26, 35, 37-39

Security Warehousing Co. v. Hand (C. C. A. 7th), 143 Fed. 32 (1906) 26, 27, 28, 29, 35-37

Spanish-American Cork Products Co., Re (C. C. A. 4th), 2 Fed. (2d) 203 ..... 9, 27, 28, 29, 39

Union Trust Co. v. Wilson, 198 U. S. 530, 25 S. Ct. 766, 49 L. Ed. 1154 (1905) 25, 26, 45

Williams v. First National Bank, 150 Tenn. 15, 261 S. W. 973 (1924) 8, 28, 39, 40

TABLE OF TEXTS

Bankruptcy Act, Sec. 67, 11 U.S.C.A., Sec. 107 8

67 Corpus Juris 486, Sec. 36 ..... 26, 27

Negotiable Warehouse Receipts Act, Williams Tennessee Code, Sec. 7587 ..... 27, 43

Uniform Laws Annotated, Vol. 3, p. 83 27

Uniform Warehouse Receipts Act, Sec. 2 (Adopted in Ill., Ark., Tenn. and Texas) 31

Uniform Warehouse Receipts Act, Sec. 50 (Adopted in Ill., Ark., Tenn. and Texas) 26

U.S.C.A. Title 28, Sec. 347 12

Williams Tenn. Code, Vol. 5, Sec. 7533-a 31, 42

Williams Tenn. Code (1932), Sec. 7544 43-44

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PETITION OF A. B. PITTMAN, TRUSTEE, NATIONAL COTTONSEED PRODUCTS CORPORATION, BANKRUPT, FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

To the Honorables, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, A. B. Pittman, Trustee, National Cottonseed Products Corporation, Bankrupt, respectfully submits his petition for a writ of certiorari to review the decree of the United States Circuit Court of Appeals for the Sixth Circuit in the above entitled case, entered March 4, 1941.

Summary Statement of The Matter Involved.

The question here presented arises out of a decree of the District Court awarding to three banks, creditors of the Bankrupt, and named as respondents here, the sum

of $1,335,980.22. The fund awarded to the banks represented the proceeds of substantially all of the Bankrupt's assets, except physical properties securing a first mortgage far in excess of their value, and $143,000.00, being the proceeds derived from the sale of the Bankrupt's cottonseed products inventory.

Proceedings in District Court.

Pleadings and Issues.

The bankrupt filed a petition on January 23, 1935, ostensibly for the purpose of seeking the benefit of the provisions of Section 77-b of the Bankruptcy Act. The petition averred that the bankrupt's business was substantially that of milling and crushing cottonseed and manufacturing products necessarily and customarily resulting from such an operation; that all of the bankrupt's physical properties were mortgaged to secure outstanding bonds in the amount of $1,216,500.00; that substantially all of its remaining assets, consisting of cottonseed and cottonseed products, notes receivable and accounts receivable, were pledged to the creditor banks; that it had a comparatively small amount of free assets "of no substantial value"; and the petition reiterated that the bankrupt was "without any prospect" of being able to pay past due interest on its mortgage debt and the large indebtedness to unsecured creditors (Vol. 1, pps. 11-16). On the same day an order was entered approving the petition and appointing temporary trustees (Vol. 1, p. 24). The cause was referred to the Master on March 18, 1935, and all creditors were required to file their claims with him (Vol. 1, p. 34). It being apparent that because of the debtor's hopelessly insolvent condition, no reorganization could be effected, an order was entered on April 11, 1935, adjudicating that the bank-

rupt was insolvent; that the appraised value of the mortgaged properties was $707,500.00; that the bonds secured by the mortgage amounted to the sum of $1,216,500.00, with unpaid interest from July 1, 1934; that a plan, theretofore submitted and filed, which contemplated the transfer of the mortgaged properties to a corporation for the benefit of bondholders be submitted to bondholders; that the Trustee proceed with liquidation of all other assets as an ordinary bankruptcy case (Vol. 1, pps. 37-41). The bondholders were awarded a deficiency judgment of $509,000.00 (Vol. 2, p. 410).

The respondent banks filed claims in the bankruptcy proceeding, asserting liens on the Bankrupt's cottonseed inventory and its cottonseed products inventory, and to proceeds derived therefrom, by virtue of so-called field warehouse receipts and trust receipts. (Rec. V. 1, p. 42-68.) Petitioner filed objections to the banks' claims, asserting that the banks were not entitled to any lien upon the cottonseed, because the so-called field warehouse receipts and other instruments through which they claimed a lien were void under state law, and were not, therefore, enforcible in bankruptcy (Rec. V. 1, pps. 70-73, 79-81, 92-96).

The Trustee petitioner's insistence was and is that these receipts did not vest in the banks any lien, because the Bankrupt retained possession and control of the cottonseed and products inventory, and at no time did the banks or the field warehouseman take any actual, open and exclusive possession. The constantly changing mass of seed was left on the premises at the manufacturing plants of the Bankrupt. In addition there was a written agreement, by the terms of which the Bankrupt was to consume the inventory in its processing operations, and market the by-products

derived therefrom, and repay the banks out of funds derived from the normal operation of its business. Petitioner insisted that the field warehousing agreement existed only on paper, and was only intended to afford the banks an unrecorded secret lien; that while the receipts used were negotiable in form and contained all of the elements prescribed by the statutes, they vested no right in the holders, because they did not describe any specific property, but simply called for specific quantities out of a fluctuating whole; and further, because by express agreement and understanding between the banks, the Bankrupt and the warehouseman, the receipts were not intended to cover cottonseed at the locations stated in the receipts, but attempted to indiscriminately pass title to the products or seed at any one of ten mills located in eight cities, and four States.

The cause having been referred to a special master, he was directed to take proof and report findings of fact and conclusions of law on the issues made by the banks' claims and the Trustee's objections thereto. The Master took several thousand pages of testimony and filed a complete report, in which he made specific findings of evidentiary facts and separate conclusions. (Rec. V. 2, pp. 349-357, 360-361, 364, and 368-370.) After finding every fact essential to establish the invalidity of the lien under the State law, and under the holding of this Honorable Court in Security Warehousing Company v. Hand, 206 U. S. 415, 27 S. Ct. 720, 51 L. Ed. 1117, as petitioner sees it, the Master reached the conclusion that despite those facts, the receipts on seed were valid, and vested a lien in the banks enforcible in bankruptcy. (Rec. V. 2, p. 368-370.) Petitioner filed exceptions to the Master's conclusion but not to the fact findings.

The District Judge overruled the exceptions and sustained the receipts without finding any facts in conflict with the facts found and reported by the Master, and without filing any opinion expressing his reasoning. (Rec. V. 1, p. 279-280.)

Petitioner appealed to the United States Circuit Court of Appeals for the Sixth Circuit, and there assigned as error the action of the District Judge in sustaining the validity of the liens. Other holdings of the District Court were challenged, but we do not conceive that they are open for review by this Honorable Court.

The United States Circuit Court of Appeals unquestionably accepted the undisputed statement of facts found and reported by the Master, but it concurred in the holding of the lower court that on that state of facts the receipts were valid.

At the instance and request of the Trustee the Master reported in detail the Evidentiary Facts, going to the very heart of this question (Vol. 2, pps. 349-357, 360-361 & 364). Those reported facts substantially show that the bankrupt, being insolvent and wholly without operating funds, entered into an arrangement with the banks, with whom it was closely allied and whose officers and stockholders practically owned it, whereby the banks would lend it such funds as might be necessary to carry on its actual operations and enable it to stay in business and obtain credit from others, but at the same time retain for the banks a secret lien upon every substantial item of the bankrupt's properties and assets (Vol. 2, pps. 406-411). After two local warehouse companies had declined to continue such a field warehousing system upon advice of counsel (Exhs. 77 & 96), a

deal was made with the Nashville Warehouse and Elevator Corporation of Nashville, Tennessee, which had no storage facilities in Memphis or at any other place where the bankrupt operated, substantially as follows,—a lease was executed on all the bankrupt's properties providing: a yearly rental of Ten ($10.00) Dollars and Ten (10c) Cents per ton for all seed warehoused; sole and exclusive possession by the warehouse company; an absolute segregation of the warehoused property; the appointment of a custodian at each mill; a fidelity bond on each custodian; and the issuance of warehouse receipts by an employee of the warehouse company from the head office of the bankrupt, those receipts to be pledged with the banks (Vol. 2, pps. 349-350). That was the arrangement as it existed on paper, but the undisputed proof showed and the Master reported that no rent was ever paid, the leases were not recorded any place, no walls, barriers, or partitions were ever erected, and the bankrupt's employees continued to use the premises and handle the seed and products exactly as before. Employees of the bankrupt were appointed custodians and the bankrupt continued to pay their salaries and they continued to work for the bankrupt exactly as before, except that each day the custodians would take from the bankrupt's records a notation of quantities on hand and send this in a report to a representative of the warehouse company stationed in the bankrupt's head office (Vol. 2, p. 350). The undisputed proof was and the Master reported that the bankrupt paid every expense in connection with the warehousing arrangement and the warehouse company required a signed agreement relieving it of every duty of a warehouseman (Vol. 2, p. 351 & Exh. 33 & 325).

During the entire period in question, the cottonseed inventory was in the bankrupt's seed houses, handled exclusively by the bankrupt's employees, constituted the bankrupt's inventory, and it was contemplated by the banks, the bankrupt and the so-called field warehousemen, that the cottonseed should be consumed by crushing and the products exhausted by sale (Vol. 2, pps. 351-352 & 364). From those facts it inescapably follows that the so-called warehousemen did not have the actual, open and exclusive possession of the cottonseed inexorably required by law to sustain this character of lien. After finding the above facts in favor of the Trustee, the Master however recommended that the banks' claims to a lien on cottonseed by virtue of the warehouse receipts be sustained because the bankrupt and the field warehousemen went through a lot of forms. These forms were emptied of significance by contrary intention and action of the parties. The bankrupt's seed inventory was sold for $1,335,980.22, and the entire amount was awarded to the banks. It was held that the pledge of the field warehouse receipts gave the banks a lien on the cottonseed inventory to the exclusion of all other creditors.

The Master, the District Judge and the United States Circuit Court of Appeals, all held that the warehouse receipts covering the Bankrupt's products inventory were fraudulent in law and void, and insufficient to create a lien valid under State law. The warehousing arrangement and the receipts on products were substantially identical with the warehousing arrangement and receipts on cottonseed, except that the Master found that the signs on the products houses were insufficient to meet the requirements of the law. Insofar as the possession required by law is concerned, there was no difference in the warehousing of either seed or products.

The question desired to be presented to this Honorable Court for decision is whether the District Court and the United States Circuit Court of Appeals arrived at the correct conclusions with respect to the undisputed facts found and reported by the Master, to which neither side filed exceptions. It is petitioner's insistence that those facts conclusively establish the invalidity of the alleged lien under the controlling State law, and that the decisions of the lower courts are in direct conflict with the opinion of this Honorable Court in the last reported decision on the question. (Security Warehousing Company v. Hand, 206 U. S. 415, 27 S. Ct. 720, L. Ed. 1117.)

Reasons Relied On for Allowance of The Writ.

The only liens sustainable in bankruptcy against the Trustee in Bankruptcy, are those valid under State law. (Bankruptcy Act, Sec. 67, 11 U.S.C.A. Sec. 107; Benedict v. Ratner, 268 U. S. 353, 45 S. Ct. 566 (1925), 69 L. Ed. 991.)

The decision of the United States Circuit Court of Appeals in this case, when applied to the undisputed facts found and reported by the Master, is in conflict with the uniform decisions of the Supreme Court of Tennessee. (Williams v. First National Bank, 150 Tenn. 15, 261 S. W. 973, and cases therein cited.)

The United States Circuit Court of Appeals has held in this case that the taking of leases, appointment of the Bankrupt's employees as custodians, and the other forms gone through, give validity to the liens, although the undisputed facts reported by the Master, and to which neither side filed exceptions, establish to our minds that neither the warehouseman nor the creditor banks ever had actual,

open and exclusive possession of the cottonseed. In addition there was a written agreement, by the terms of which the debtor was to consume the entire seed inventory by crushing and exhaust the products by sale in the ordinary course of business. The holding is in conflict with the last reported opinion of this Honorable Court, where it was held that an identical arrangement was void under State law the same in principle as the Tennessee law. (Security Warehousing Company v. Hand, 206 U. S. 415, 27 S. Ct. 720, 51 L. Ed. 1117.) This Honorable Court there held that such an arrangement as the lower court has sustained in this case was nothing more than a pretense and a sham, and wholly inadequate to sustain the lien.

It will appear from a large number of decisions by the various United States Circuit Courts of Appeal that the application of the principles announced by this Honorable Court in the Hand case have in some instances seemingly been disregarded, in others the decision has been passed up by mere reference to it without applying the holding there announced, while in the majority it has been followed. The various applications of the rule there announced have resulted in uncertainty and conflicts in the various Circuits, and the decision in this case has resulted in a conflict between the Sixth Circuit and other Circuits, namely, the Second, Third, Fourth and Seventh Circuits. (Pittman, Trustee, v. Union Planters National Bank and Trust Company, et al., C.C.A. 6th, 118 Fed. (2d) 211; Re: Coats, Bennett & Reidenbach, C.C.A. 2d, 12 Fed. (2d) 497; Fourth State Nat'l Bank v. Milboune Mill Co.'s Trustee, C.C.A. 3rd, 172 Fed. 177; Re: Spanish-American Cork Products Co., C.C.A. 4th, 2 Fed. (2d) 203; In Re: Rogers, C.C.A. 7th, 125 Fed. 169; American Can Co. v. Erie Preserving Co. (D.C.), 171 Fed. 540, C.C.A. 7th, 183 Fed. 96.)

In the cases relied on the courts were dealing with State law like the Tennessee law and applying it in bankruptcy cases. It is submitted that the widespread and rapidly increasing use of various schemes and devices to circumvent the rule against secret liens and the laxity of the various courts in enforcing that rule, requires a restatement of its position by this Honorable Court, in order that there may be more certainly with respect to the status of such schemes and devices in bankruptcy.

The United States Circuit Court of Appeals, in its opinion, has construed the Uniform Negotiable Receipts Act, as adopted in Tennessee, to mean that the provisions required by that act to be contained in the receipt, and especially, statement of the location of the goods stored, may be vitally altered by oral and secret agreement between the receipt holder and the warehouseman, in complete disregard of the rights of creditors or a trustee in bankruptcy of the depositor. This act is in force in many States, and its construction is, therefore, a matter of broad general importance, especially in the administration of the Bankruptcy Act in the Federal Courts. Especially is the decision sought to be reviewed here replete with potential dangers, when the required statement as to location of the goods is so important an element of possession by the alleged warehouseman; and this latter question is invariably acute in the cause of so-called field warehousing. At least, it should be if the rights of creditors are given proper regard.

A certified copy of the entire record of said case in the Circuit Court of Appeals is hereby furnished and filed with this petition, in accordance with Rule 38 of this Honorable Court.

Prayer for Writ.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Sixth Circuit, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, "No. 8406, A. B. Pittman, Trustee, National Cottonseed Products Corporation, Bankrupt. Appellant v. Union Planters National Bank and Trust Company, et al., Appellees"; and that said judgment of said United States Circuit Court of Appeals for the Sixth Circuit may be reversed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

A. B. PITTMAN, TRUSTEE, NATIONAL COTTONSEED PRODUCTS CORPORATION, BANKRUPT,

LOWELL W. TAYLOR,
LARRY CRESON,
Attys. for Petitioner.